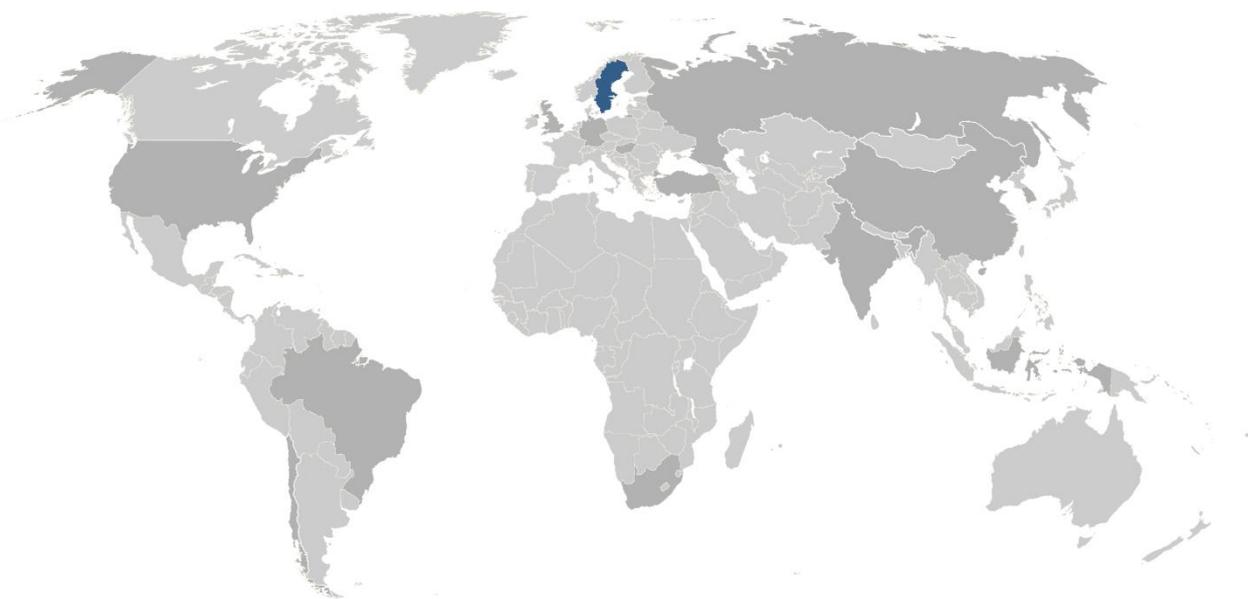


# Managing the Crisis | Sweden Country Report

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## 1. Risk Exposure at the Outset of the Crisis

- What was the structure of demand (e.g., share of private/state consumption, gross capital formation, exports and imports in GDP/GNI)?
- To what extent was the economy exposed to macroeconomic imbalances (e.g., foreign debt, trade or fiscal imbalances)?
- Was/is the financial system primarily bank- or market-based?

Economic structure and macroeconomy

The Swedish economy boomed during the past decade. Economic growth was above the European average, inflation comparatively low, and employment increased steadily. On the one hand, this performance was enabled by economic and fiscal policy measures put in place after the Swedish banking crisis in the early 1990s. On the other hand, this boom benefited from the increasing openness of the Swedish economy and the international rise of information technology (IT) industries. As a consequence, the vulnerability of the Swedish economy on the eve of the international financial crisis was very high. “Having surfed the earlier global wave, Sweden has been hit hard by its crash.”<sup>1</sup>

The Swedish model reveals some distinctive features:<sup>2</sup>

- The Swedish model is based upon a distinctive public-private mix. High taxes, intensive public spending and high levels of public employment are features of this particular political economy. Revenues and public spending each have been over 59 percent of GDP in recent decades. The Swedish state employed over 28 percent of the total labor force in 2005.<sup>3</sup>
- The Swedish model received much attention for its openness to foreign markets and its ability to combine this dynamic openness with social cohesion and a universal welfare state. Sweden differs from many OECD countries in regard to low corruption, high trust embedded in Swedish society as well as a highly educated labor force.<sup>4</sup>

Beyond the strong state, the Swedish economy is oriented toward world markets. The value of exports and imports combined are around 100 percent of the country’s GDP, and the volume of Swedish exports is always larger

<sup>1</sup> IMF, “Sweden: 2009 Article IV Consultation – Staff Report” (2009): 3, <http://www.imf.org/external/pubs/ft/scr/2009/cr09247.pdf> (accessed November 12, 2009).

<sup>2</sup> cf. OECD, “Economic Survey: Sweden,” (2008).

<sup>3</sup> OECD, “Country Note: Sweden,” *Government at a Glance* (2009): <http://www.oecd.org/dataoecd/35/40/43925756.pdf> (accessed October 10, 2009).

<sup>4</sup> OECD, “Economic Survey: Sweden,” (2008).

than that of imports.<sup>5</sup> More than 35 percent of all exported goods and services are electronic equipment and machinery, and approximately 15 percent are intermediate capital goods. In recent years, business services have expanded substantially. These goods benefited from the international boom in European emerging markets as well as in Nordic neighbor countries.<sup>6</sup> Sweden's largest share of exports is directed toward advanced economies, especially toward the neighbor countries of the European Union (40% of total exports). Since the mid-1990s, exports into European emerging markets and especially into the Baltic region have increased considerably.

Since the 1990s, private household final consumption expenditures have represented approximately 50 percent of GDP. Since 2005, a slight decline in this figure has been observable. Government final consumption expenditure has increased since the 1950s, reaching a high of about 30 percent of GDP. Since the 1990s, however, it has decreased steadily to reach approximately 25 percent of GDP in 2008.<sup>7</sup>

Swedish governments gradually deregulated the domestic financial market beginning in the mid-1980s, subsequently allowing Swedish banks to enter Eastern Europe markets, especially those in the Baltic region. During the past decade, Swedish banks profited from the economic boom in Eastern Europe, which generated high income flows. In 2007, about five percent of the country's total lending was to borrowers in the Baltic states. The domestic financial market is mainly bank-based and dominated by four banks, which together control 80 percent of the banking market. Approximately 30 percent of total lending is directed toward foreign companies. The remaining 70 percent is equally distributed between domestic companies, domestic households and foreign households.<sup>8</sup>

- What was the government's economic record (e.g., growth, unemployment rate, inflation and fiscal position) prior to the crisis?
- What was on the economic agenda prior to September 2008 (e.g., anti-inflation, efficiency-oriented, redistributive, supply vs. demand-side policies)?

Policy priorities  
prior to crisis

After the September 2006 elections, a four-party "bourgeois," or center-right coalition government was established under the leadership of Conservative Prime Minister Lars Reinfeldt.<sup>9</sup> As major goals, the new government in-

<sup>5</sup> Comprehensive surveys of economic development in Sweden are available in English from the Statistiska centralbyrån at: [http://www.scb.se/Pages/List\\_259034.aspx](http://www.scb.se/Pages/List_259034.aspx) (accessed October 10, 2009).

<sup>6</sup> IMF, "Sweden 2009: Staff Report," (2009): 10.

<sup>7</sup> OECD, "Economic Survey: Sweden," (2008).

<sup>8</sup> OECD, "Economic Survey: Sweden," (2008): 26, 30.

<sup>9</sup> The Conservative Party is the largest party in the coalition, followed by the Center Party, the Liberal People's Party and the Christian Democrats.

tended to further increase employment and to decrease the benefit dependency rate by a significant amount. Tax reductions were promised, though the executive repeatedly stated that tax reductions should never endanger the major goal of maintaining stable and balanced public budgets.

The open unemployment rate decreased from its peak of 9.3 percent in 1994 to 6.1 percent in 2008. For 2009 and the near future, a rise in open unemployment is forecasted. Currently, the government expects the open unemployment rate to rise to approximately 11 percent in 2010. Employment rates are high from a comparative point of view; in 2008, approximately 76 percent of all Swedes between the ages of 16 and 64 were employed. Employment growth has been robust during the past decade, and the government and the Riksbank (Sweden's central bank) have successfully contained inflation. Since 1995, inflation in Sweden has been lower than in the euro area.<sup>10</sup>

Economic growth, dynamic labor markets and a stable financial framework have been the country's fundamental economic pillars since the late 1990s. Financial policy has effectively been able to reduce public debt and consolidate public budgets. In 1997, the (Social Democratic) government introduced strict rules for financial policy-making. Since that time, the government has been required to present a medium-term fiscal framework, designed to stabilize policy projections. Furthermore, the budgeting process was centralized. In 2000, a Social Democratic government introduced a budget surplus target and balanced budget requirements for local governments. The main fiscal target is to reach a general government surplus of one percent of GDP over the course of the business cycle. The balanced budget requirements force local governments to offset temporary deficits with surpluses within three years.<sup>11</sup> In 2007, the center-right government installed a Fiscal Policy Council (Finanspolitiska Rådet) tasked with monitoring the fulfillment of fiscal targets.

Taken together, the net-lending targets and expenditure ceilings have been successfully met. Public debt was reduced from approximately 70 percent of GDP in the mid-1990s down to slightly below 38 percent of GDP in 2008.<sup>12</sup> This consolidation of public budgets and reduction in public debt has been "achieved through expenditure restraint rather than higher taxation."<sup>13</sup> Sweden has shown among the largest growth in net financial assets of any OECD country.

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<sup>10</sup> cf. OECD, "Economic Survey: Sweden," (2008); IMF, "Sweden 2009: Staff Report."

<sup>11</sup> cf. OECD, "Economic Survey: Sweden," (2008): Chapter 2.

<sup>12</sup> IMF, "Sweden 2009: Staff Report," 9; OECD, "Economic Outlook 1/2009," 313.

<sup>13</sup> OECD, "Economic Survey: Sweden" (2008): 52, 55.

During the past decade, social democratic as well as center-right governments have agreed on the need to stabilize fiscal policies and reduce public debt. The major remaining differences between the political blocs are centered on taxation, privatization and deregulation. Following the election in 2006, the center-right coalition government reduced taxes on several occasions and began a process of privatizing state-owned companies. As a main pillar of these reforms, the government introduced an earned income tax credit, which took effect in January 2007. Additionally, the deregulation of distinctive markets (telecommunications, railway, health services) has been pushed forward. The center-right coalition has sought to enhance efficiency and competitiveness with these measures.

- How stable was the executive branch in the years/months prior to September 2008 (e.g., credibility/legitimacy of leaders/parties in government, cabinet stability/reshuffles, parliamentary/electoral support)?
- How much room did fiscal conditions provide for a major stimulus (e.g., budget surpluses/deficits, conditions for issuing additional treasury bonds)?
- How much room was there for monetary policy initiatives (e.g., pre-crisis level of interest rates, required reserve ratios, flexibility of foreign exchange rate regime)?

Executive, fiscal & monetary capacities to respond to downturn

The current center-right coalition lost ground in public opinion polls immediately after the election in 2006. This was partly caused by several early cabinet reshuffles (for a variety of reasons). In spring 2008, the opposition (i.e., the Social Democratic Party, the Green Party and the Left Party) had a lead over the center-right parties by 20 percentage points in the polls. Since September 2008, this trend has reversed. In summer and fall 2009, political competition between the two political blocs was a neck-and-neck race.<sup>14</sup> Internally, the four parties in government have had some conflict; however, in every instance, the parties have agreed to maintain the coalition intact. This is remarkable from a historical perspective, as programmatic differences between the parties of the right have been so large that other center-right coalitions in Swedish history have proved rather unstable. This current stability can be explained through the intensified levels of cooperation between the center-right parties, initiated by the Conservative Party in 2003.

The Swedish economy entered the global recession in a sound position. Because of solid public finances and a strong fiscal framework, the country has had considerable maneuvering room with which to counteract the economic downturn. In contrast to other OECD countries, public debt is relatively low. Net lending during the past decade was additionally comparatively low. In fact, Sweden is one of a few OECD countries which on the eve of financial

<sup>14</sup> Data are taken from: [http://www.synovate.se/Templates/Page\\_195.aspx](http://www.synovate.se/Templates/Page_195.aspx) (accessed October 15, 2009).

turmoil had assets in excess of liabilities (assets were the equivalent of 20% of GDP in 2007). “In comparison to other OECD countries, it (Sweden) has (...) achieved one of the largest improvements in net financial assets over the last decade.”<sup>15</sup>

The Swedish central bank (Riksbank) has been fully independent of the government since 1999. Its primary goals are to conduct monetary policy and to maintain financial stability. As a “nominal anchor” for monetary stability, the Riksbank targets an annual change in the consumer price index of two percent.<sup>16</sup>

Interest rates in Sweden by and large follow the EU pattern. On the eve of the financial crisis, long-term interest rates were approximately four percent, in line with the EU average.<sup>17</sup>

During the crisis in the early 1990s, the Riksbank vehemently defended the fixed exchange rate regime, albeit without success. Since then, the central bank has followed a floating exchange rate regime.

- To what extent has the country been exposed to global financial market risks, particularly contagious/toxic financial instruments (e.g., open capital account, floating or pegged/fixed currency)?
- How important was/is the financial sector for the national economy? What was/is the extent of interdependence between the financial sector and real economy?
- To what extent was the economy integrated into regional/global trade flows? How dependent was the economy on foreign demand for manufactures and commodities?
- Did property, equity or other markets display excessive growth and a bubble-like situation prior to September 2008?
- In what condition was the banking sector (e.g., size/structure of banking sector, non-performing loans, capital adequacy ratios of major banks, if available)?

Exposure to specific market and trade risks

Partly because of lessons drawn from the early-1990s financial crisis in Sweden, levels of outstanding risk in the Swedish financial market were low. First, in contrast to other European countries, direct linkages between Swedish banks and U.S. banks were rather rare. However, Swedish banks were of course connected to various European banks, which in turn had intense relationships with U.S. market participants.<sup>18</sup> On the other hand, Swedish

<sup>15</sup> OECD, “Economic Survey: Sweden” (2008): 55.

<sup>16</sup> cf. Sveriges Riksbank, “Monetary Policy in Sweden” (Stockholm: 2008), [http://www.riksbank.com/upload/Dokument\\_riksbank/Kat\\_publicerat/Rapporter/2008/monetary\\_policy080707.pdf](http://www.riksbank.com/upload/Dokument_riksbank/Kat_publicerat/Rapporter/2008/monetary_policy080707.pdf) (accessed October 15, 2009).

<sup>17</sup> Sveriges Riksbank, “Monetary Policy Report, October 2009,” (Stockholm: 2009): 29-30. ([http://www.riksbank.com/upload/Dokument\\_riksbank/Kat\\_publicerat/Rapporter/2009/mpr\\_3\\_09oct.pdf](http://www.riksbank.com/upload/Dokument_riksbank/Kat_publicerat/Rapporter/2009/mpr_3_09oct.pdf) (accessed November 25, 2009).

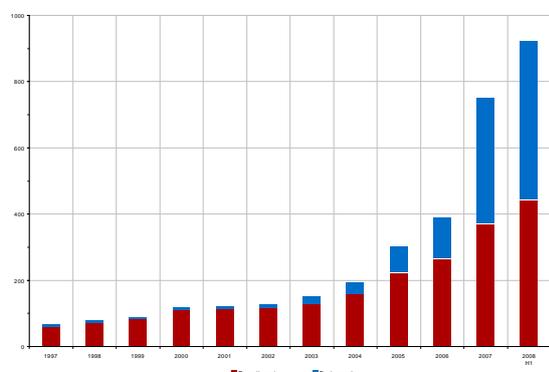
<sup>18</sup> Clas Bergström, “Finanskrisen och den svenska krishanteringen under hösten 2008 och vintern 2009.” *Rapport till Finanspolitiska rådet 2009/1* (Stockholm: 2009) <http://www.finanspolitiskaradet.se/download/18.1166db0f120540fe0498000209106/090609+Bergstr%C3%B6m.pdf>, (accessed October 5, 2009).

banks had invested intensively abroad in recent years, especially in the Baltic states. At the end of 2008, Swedish banks' equity and loan claims (mainly SEB and Swedbank) associated with their Baltic subsidiaries represented eight percent of Sweden's GDP. SEB and Swedbank loans to their Baltic subsidiaries amount to 35 percent to 45 percent of their total capital.<sup>19</sup>

The importance of Swedish banks as compared to other parts of the economy had increased in recent years. The financial market had expanded remarkably in the last several decades; total assets held by Swedish banks rose from 120 percent of GDP in the mid-1980s to 280 percent in 2008.<sup>20</sup> Since 2006, foreign liabilities and claims held by Swedish banks had also increased significantly (see Figure 1).<sup>21</sup>

The Swedish banking system entered the financial crisis in a strong position. The four largest banks, which together represent 80 percent of the total market, had solid assets in 2007 (total assets as a percent of GDP were Nordea: 120.3%; SEB: 76.5%; Handelsbanken: 60.7%; Swedbank: 52.5%). Additionally, the rate of nonperforming loans in relation to total gross loans was rather low (Nordea: 0.6%, SEB: 0.5%, Handelsbanken: 0.1%, Swedbank: 0.1%).<sup>22</sup>

Figure 1: Banking system's assets as a percentage of GDP (1997 - 2008)



Source: Sveriges Riksbank, "Slides to Financial Stability Report 2008:2," *Financial Stability Report 2008*, <http://www.riksbank.com/templates/ItemList.aspx?id=28151> (accessed October 15, 2009).

The financial sector and the real economy are interdependent. However, Swedish firms are embedded into the European financial market, too. Hence, the Swedish financial market is fully globalized, and financial activities in-

<sup>19</sup> IMF, Sweden 2009: Staff Report (2009): 29.

<sup>20</sup> SCB: *The Swedish Economy. Statistical Perspective, 1/2009* (Stockholm: 2009): 20.

<sup>21</sup> SCB, "Financial Market Statistic, September 2009" (Stockholm: 2009),

[http://www.scb.se/statistik/publikationer/FM5001\\_2009M09\\_BR\\_FM5001BR0910ENG.pdf](http://www.scb.se/statistik/publikationer/FM5001_2009M09_BR_FM5001BR0910ENG.pdf).

<sup>22</sup> IMF, Sweden 2009: Staff Report, 14.

creased significantly during the past decade.<sup>23</sup> As a consequence, this increased the interdependence between financial markets and the real economy. As Riksbank Deputy Governor Lars Nyberg stated as early as 2002 with respect to the development of Sweden's financial markets: "Increased saving and financing in market-listed instruments have made households and companies more dependent on the safe and efficient functioning of the financial markets. This could mean that the effects of disturbances from the financial system on the real economy could increase in the long term if regulatory frameworks and supervision are not adapted sufficiently rapidly."<sup>24</sup>

As mentioned above, the Swedish economy is highly integrated into European markets. As a consequence, the Swedish economy is highly dependent on foreign demand for manufactures and commodities. The Swedish economy is also highly dependent on the functioning of financial systems, given the increased openness of the Swedish financial system during the last decade.

The overall economic situation was balanced on the eve of financial crisis. Housing markets were tight, especially in the main cities. Nevertheless, no local economic observers or economic research institutes mentioned the danger of domestic bubble-like situations.

- Did policymakers/executive agencies have any experience in handling financial crises? Did this experience play a role in the 2008-09 policy response?
- Were there independent regulatory institutions or prevention/response schemes in place to contain financial risks?
- Were there internal veto players (e.g., federalist powers, courts) or international obligations that thwarted swift action on the part of the government?
- Have executive powers been extended in times of crisis? Has this been based on formal or informal mechanisms?

Structural or policy advantages and disadvantages

Swedish policymakers had to manage a severe banking crisis in the early 1990s. Today, their history of crisis management is admired by some observers, and some even argue that this experience could serve as a blueprint for managing the current financial crisis. In the early 1990s, Swedish policies were largely implemented ad hoc. However, in retrospect, we can regard the core of the crisis resolution as comprising the following features.<sup>25</sup>

<sup>23</sup> Sveriges Riksbank, "The Swedish Financial Market" (Stockholm: 2009), [http://www.riksbank.com/upload/Dokument\\_riksbank/Kat\\_publicerat/Rapporter/2009/finansmarknaden\\_2009\\_eng2.pdf](http://www.riksbank.com/upload/Dokument_riksbank/Kat_publicerat/Rapporter/2009/finansmarknaden_2009_eng2.pdf) (accessed October 20, 2009).

<sup>24</sup> Lars Nyberg, "Financial Disturbances and the Real Economy," (2002) <http://www.riksbank.com/templates/speech.aspx?id=6330> (accessed October 15, 2009).

<sup>25</sup> Lars Jonung, "The Swedish model for resolving the banking crisis of 1991 - 93. Seven reasons why it was successful," *European Economy, Economic Papers*360 (Brussels: 2009)

Despite political competition, there was from the beginning of the crisis broad political unity between government and opposition. The government declared that depositors and other counterparts of Swedish commercial banks and financial institutions would be protected from future losses. Then, the following measures were implemented swiftly. The first measure was to introduce a special Bank Support Authority, Bankstödsnämnd, with open-ended funding. This authority demanded full transparency from all banks that claimed financial help. The Authority differentiated between the commercial banks and created a “bad bank.” Overall, the Authority made sure to save the banks, not the owners of the banks. The owners of banks were forced to absorb losses, a policy which in turn fostered public acceptance of the approach to crisis management. Finally, macroeconomic policies facilitated the recovery. The most important source for recovery was the depreciation of the Swedish krona (by approximately 30%), combined with an expansive fiscal policy. In response to these measures, the economy recovered very quickly, the pressure on the banking system lessened and balance sheets were strengthened.

During the current crisis, policymakers in Sweden held the lessons learned in the early 1990s (at least partially) in mind. However, policymakers are aware that the current financial crisis is different in some aspects. First, the Swedish crisis in the early 1990s was a local phenomenon (or a Nordic one), while the current crisis is global. Hence, the Swedish economy is highly dependent on international developments today. Second, the Swedish option of a depreciation of the krona, spurring an export-led recovery, is currently not available to all countries in the world. Finally, the financial system was less sophisticated in the early 1990s. Today’s crisis was induced by several actors on the financial market, not simply banks, all of which dealt with highly differentiated products. Moreover, in 1990s Sweden, public trust in the financial market and in financial actors was high, in sharp contrast to the situation today.

The Swedish central bank (Sveriges Riksbank) and the Swedish Financial Supervisory Authority (Finansinspektionen) supervise the financial market. While the Riksbank is formally independent from the government, the Finansinspektionen is accountable to the Ministry of Finance. The third institution which monitors the financial system is the National Debt Office (Riksgälden). This authority has the duty to administer the public debt, including the ability to borrow in the market or invest any liquidity surplus in the market.

Sweden's democratic system lacks powerful (domestic) veto players. The executive is able to push policies through the unicameral Riksdag. The center-right government has had a (slim) majority since the election in 2006; however, the governing coalition is internally very cohesive. Policy-making in Sweden is embedded into the formal framework of the European Union. From the beginning of the crisis, the Swedish government emphasized the need to coordinate crisis management activities on a European level. This was partly reinforced by the fact that Sweden held the presidency of the European Union in the second half of 2009.

Executive powers have not been extended in times of crisis. Political crisis management in Sweden rests on formal as well as informal cooperation between the government, the parliament and the central bank. Since the 1990s, however, cooperation with powerful interest organizations such as trade unions and employers' associations has declined. Crisis management in Sweden has been dominated by the powerful executive.

- How strongly has the national economy been hit during the period under review? Where has it been hit most severely thus far (e.g., growth rate, production, trade, employment)?

Initial impact of economic downturn

Given the high openness of the Swedish economy and the increasing openness of the financial market, it is not surprising that the country's economy was hit fast and hard by the unfolding financial crisis. Swedish exports began to plummet during the second quarter of 2008 in reaction to the financial crisis, with a further significant acceleration in this decline in the fourth quarter of 2008. This amounted to a 10 percent drop in exports as compared to the corresponding quarter of 2007.<sup>26</sup> Along the same lines, consumer confidence was weakened, which resulted in lower consumption and higher savings levels.<sup>27</sup> Household consumption decreased by three percent, the first downturn since 1993. Obviously, during the latter part of 2008, households in Sweden reduced their spending and increased savings. Despite a slight increase in household disposable income (1%), the household saving rate in 2008 was 7.4 percent of disposable income—the highest share since the early 1990s.<sup>28</sup> The single biggest cut in demand from households affected passenger car sales.<sup>29</sup>

<sup>26</sup> Statistiska centralbyrån, *The Swedish Economy, Statistical Perspective*, Number 1 (2009): 3 ([http://www.scb.se/Grupp/Teman/Sveriges\\_Ekonomi/\\_Dokument/Econreportq408.pdf](http://www.scb.se/Grupp/Teman/Sveriges_Ekonomi/_Dokument/Econreportq408.pdf) (accessed November 12, 2009)).

<sup>27</sup> IMF, "Sweden 2009: Staff Report."

<sup>28</sup> Statistiska centralbyrån, *The Swedish Economy, Statistical Perspective*, Number 1 (Stockholm: 2009): 3 ([http://www.scb.se/Grupp/Teman/Sveriges\\_Ekonomi/\\_Dokument/Econreportq408.pdf](http://www.scb.se/Grupp/Teman/Sveriges_Ekonomi/_Dokument/Econreportq408.pdf) (accessed November 12, 2009)).

Real GDP stalled in the first half of 2008.<sup>30</sup> This slowdown was induced by weak exports and weak international investment activities. This affected Swedish exports very significantly, because exports to a large degree consist of investment products. Between the fourth quarter of 2007 and the fourth quarter of 2008, GDP fell by 4.8 percent. However, GDP fell by a total of 0.2 percent in full-year 2008. An involuntary decrease in industrial inventories contributed 1.8 percentage points to this downturn. Current assessments from enterprises as to the size of inventories of finished goods have not been so negative since the crisis of 1991.<sup>31</sup>

The financial crisis also caused a fall in Swedish business production of historic levels. Beginning in the last quarter of 2008, the Swedish manufacturing industry was affected most sharply, with difficulties remaining today. The engineering industry was hit most intensively, while the chemical, wood and paper industries weathered the crisis somewhat better. This pattern has been mirrored in employment patterns. Growth in the number of hours worked in the service sector stopped; however, a very sharp decline occurred among goods producers.<sup>32</sup> This deterioration immediately led to increasing numbers of layoffs. The number of job losses increased from 14,000 in the second and third quarters combined to about 57,000 in the fourth quarter of 2008. Employment declined in the manufacturing industries (and was concentrated intensively on permanent employees). Even employment in the public sector declined substantially. However, this trend had been seen as early as the beginning of 2007.<sup>33</sup> Employment losses have been concentrated in the north of the country and in East Middle Sweden. In Stockholm, for example, the number of employees actually showed some growth between the third and fourth quarters of 2008.<sup>34</sup> These dynamic changes are not captured by official data reporting on the whole of 2008. In

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<sup>29</sup> Statistiska centralbyrån, *The Swedish Economy, Statistical Perspective*, Number 1 (Stockholm: 2009): 9,

[http://www.scb.se/Grupp/Teman/Sveriges\\_Ekonomi/\\_Dokument/Econreportq408.pdf](http://www.scb.se/Grupp/Teman/Sveriges_Ekonomi/_Dokument/Econreportq408.pdf) (accessed November 12, 2009).

<sup>30</sup> OECD, "Economic Survey Sweden" (2008).

<sup>31</sup> Statistiska centralbyrån, *The Swedish Economy, Statistical Perspective*, Number 1 (Stockholm: 2009): 6, 14

[http://www.scb.se/Grupp/Teman/Sveriges\\_Ekonomi/\\_Dokument/Econreportq408.pdf](http://www.scb.se/Grupp/Teman/Sveriges_Ekonomi/_Dokument/Econreportq408.pdf) (accessed November 12, 2009).

<sup>32</sup> Statistiska centralbyrån, *The Swedish Economy, Statistical Perspective*, Number 1 (Stockholm: 2009): 15-16

[http://www.scb.se/Grupp/Teman/Sveriges\\_Ekonomi/\\_Dokument/Econreportq408.pdf](http://www.scb.se/Grupp/Teman/Sveriges_Ekonomi/_Dokument/Econreportq408.pdf) (accessed November 12, 2009).

<sup>33</sup> Statistiska centralbyrån, *The Swedish Economy, Statistical Perspective*, Number 1 (Stockholm: 2009): 18

[http://www.scb.se/Grupp/Teman/Sveriges\\_Ekonomi/\\_Dokument/Econreportq408.pdf](http://www.scb.se/Grupp/Teman/Sveriges_Ekonomi/_Dokument/Econreportq408.pdf) (accessed November 12, 2009).

<sup>34</sup> Statistiska centralbyrån, *The Swedish Economy, Statistical Perspective*, Number 1 (Stockholm: 2009): 19

[http://www.scb.se/Grupp/Teman/Sveriges\\_Ekonomi/\\_Dokument/Econreportq408.pdf](http://www.scb.se/Grupp/Teman/Sveriges_Ekonomi/_Dokument/Econreportq408.pdf) (accessed November 12, 2009).

this larger perspective, for example, open unemployment remained stable in 2008 at 6.1 percent.<sup>35</sup>

Despite negligible exposure to U.S. assets, bank profitability fell sharply during 2008. Two of the largest Swedish banks (SEB and Swedbank), both increasingly dependant on funds from wholesale markets, and both heavily exposed to the Baltics, had to report increasing losses on their loan portfolios. The key Swedish stock market index dropped nearly 40 percent in 2008.<sup>36</sup>

Inflation rose during the first part of 2008. This was mainly fuelled by increasing prices for food, energy and household interest costs. The Riksbank lifted the policy interest rate (repo rate) three times during the first three quarters of 2008.

The financial crisis challenged Swedish monetary policy. The first signs of stress in the Swedish financial system undermined the value of the country's currency. The Riksbank saw this development as a "flight to quality,"<sup>37</sup> triggered by the global financial crisis and the subsequent flight into "secure" currencies. As a consequence, beginning in October 2008, the Riksbank accepted the krona to float freely. In fighting inflation, the Riksbank switched its policy very quickly. In the fall of 2008, the Riksbank decreased the repo rate from 4.75 percent to two percent. This was the largest reduction since 1994. The Riksbank and the National Debt Office (Riksgälden) also cooperated very smoothly in efforts to increase liquidity in the financial system. The National Debt Office issued short-term Treasury bills (up to SEK 150 billion). The Riksbank also cooperated actively with the U.S. Federal Reserve, while fuelling capital in the domestic market. As a consequence, the Riksbank's balance sheet increased from SEK 200 billion to SEK 700 billion between August 2008 and the end of that year.<sup>38</sup>

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<sup>35</sup> OECD, "Economic Survey: Sweden," (Paris: 2008): 29.

<sup>36</sup> IMF, "Sweden 2009: Staff Report," 14.

<sup>37</sup> Svante Öberg, "Sverige och finanskrisen 2009,"

<http://www.riksbank.se/pagefolders/38674/090120.pdf> (accessed November 10, 2009).

<sup>38</sup> Statistiska centralbyrån, *The Swedish Economy, Statistical Perspective*, Number 1 (2009):

21-23, [http://www.scb.se/Grupp/Teman/Sveriges\\_Ekonomi/Dokument/Econreportq408.pdf](http://www.scb.se/Grupp/Teman/Sveriges_Ekonomi/Dokument/Econreportq408.pdf) (accessed November 12, 2009).

## 2. Agenda-Setting and Policy Formulation

- When did state organs (e.g., government, central bank) begin setting a crisis response agenda? How long did it take to adopt the first crisis measures?
- Who were the driving forces (e.g., government, central bank, foreign actors, media, trade unions, employers' associations) in getting stabilization/stimulus policies started?
- Were these measures launched as executive orders or parliamentary laws? How closely did constitutional bodies (e.g., executive, legislative, central bank) cooperate?
- What kind of role did sectoral or regional lobbies play in policy formulation?

Agility and  
credibility

The Swedish government monitored international developments very closely. From the beginning of the downturn, the center-right coalition emphasized the need to coordinate domestic policy-making with policy-making in the European Union. The first signs of economic turmoil became apparent during the summer of 2008, as Swedish exports declined rapidly and Swedish consumer confidence sunk. The major Swedish stock market index fell beginning in the winter of 2007 – 2008, and the Swedish banking system had to recognize increasing loan losses. In October 2008, the Riksbank opened its public crisis management efforts by shifting to an accommodating policy stance. The policy rate was cut rapidly from 4.75 percent (September 10, 2008) to 2.00 (December 10, 2008) and finally to 0.25 (July 8, 2009). Additionally, the Riksbank allowed the Swedish krona to float freely, which led to significant depreciation.<sup>39</sup>

In October 2008, the Swedish government launched a first stabilization plan for the financial market.<sup>40</sup> Political decision-making moved quickly, although the government repeatedly emphasized that all measures had to be coordinated within the framework of the European Union. The first stabilization plan was implemented very quickly. The government announced the crisis package on October 20th, and the measures went into force on October 28th.

Political decision-making during the first part of the crisis was highly contested in the public sphere. In the fall of 2008, several individual trade unions, the blue-collar trade unions' federation (Landsorganisationen

<sup>39</sup> IMF, "Sweden 2009: Staff Report," 19.

<sup>40</sup> cf. press release from October 20, 2008, <http://www.regeringen.se/content/1/c6/11/37/16/f8d01cc9.pdf> (accessed November 13, 2009).

i Sverige, LO),<sup>41</sup> and the federation of employer's organizations (Svenskt Näringsliv, SN)<sup>42</sup> argued for far-reaching crisis measures aimed at counteracting the free fall in Swedish economic activity.<sup>43</sup>

In general, Swedish crisis management policies were developed by means of normal political patterns and institutions. Policies aimed at stabilizing the economy were mostly integrated into the budgetary process. One exception was the crisis package targeted at the automotive industries (passed in December 2008), which was implemented as an extra law. Another exception was the Extra Budget Bill of January 2009, in which expansionary policies were intensified (including an increase in active labor market policies, infrastructure investment, and tax credits for home improvement).

Nevertheless, both labor and capital groups called for further investments and demand-side policies. Even the Finanspolitiska Rådet, an autonomous government advisory board, argued on several occasions that the government should increase measures aimed at stabilizing domestic demand. During 2009, the major opposition party, the SAP, published various alternative economic stimulus proposals, partially in accord with the Left Party and the Green Party.<sup>44</sup> In broad outline, the opposition called for investing more money, especially into domestic welfare institutions.

Behind closed doors, cooperation between the government and the Riksbank functioned smoothly. Additionally, the government expanded the power of special authorities, which are tasked with coordinating economic policies between the central government and local/regional governments. In contrast to the early 1990s, the government struck no policy deals with the opposition. With its slim majority in parliament, the current coalition has not been forced to integrate opposition parties into the policy-making process.

Sectoral and regional lobbying did take place. However, the influence of specific interest organizations is difficult to assess. Since the 1990s, corporatist decision-making structures have largely vanished in Sweden. Ties between political parties and interest organizations have become looser. The

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<sup>41</sup> The crisis plan of the LO is available (in Swedish) at: [http://www.lo.se/home/lo/home.nsf/unidview/DE8AF12A5112B612C12575B40045D4F8/\\$file/LO\\_en\\_alternativ\\_krispolitik.pdf](http://www.lo.se/home/lo/home.nsf/unidview/DE8AF12A5112B612C12575B40045D4F8/$file/LO_en_alternativ_krispolitik.pdf) (accessed October 15, 2009).

<sup>42</sup> The crisis plan of the SN is available (in Swedish) at: [http://www.svensktnaringsliv.se/material/rapporter/finanskrisen-vad-nu\\_65430.html](http://www.svensktnaringsliv.se/material/rapporter/finanskrisen-vad-nu_65430.html) (accessed October 15, 2009).

<sup>43</sup> cf. the information provided by the EIRO, <http://www.eurofound.europa.eu/eiro/2008/12/articles/se0812019i.htm> (accessed June 2, 2009).

<sup>44</sup> An overview of alternative crisis policies is provided at: <http://www.socialdemokraterna.se/Var-politik/Motioner-och-rapporter/> (accessed November 22, 2009); cf. "Rödgröna skuggbudgetar: jobb, jobb, job," *Dagens Nyheter*, October 6, 2009, [www.dn.se](http://www.dn.se) (accessed October 6, 2009).

center-right coalition has no open connections to trade unions; however, we can expect close ties especially between the Conservative Party and the employers' organization (SN). Nevertheless, SN was rather critical of the government in the course of public debate.

Local and regional governments are important in the Swedish model. They provide most social services and have the right to tax.<sup>45</sup> During fall 2008 and spring 2009, several local governments demanded help from the national government. Given the gradual declines in public employment since 2000, local and regional governments warned that the economic downturn might further undermine their financial positions. Further losses of employment were predicted if the central government did not inject additional funds.

- Did policymakers actively consult domestic and/or foreign experts outside of government?
- Did the government actively seek collaboration with other governments or international organizations?
- Did the government participate in multilaterally coordinated rescue efforts?
- Was the government curtailed in its response through IMF support programs?

Consultation with external experts and openness to international collaboration

Traditionally, policy-making in Sweden depends on intensive collaboration between the ministries, various interest groups and the scientific community. Policies are prepared and discussed in official reports of the Swedish government (Statens offentliga utredningarna). During the crisis, the policy-making pattern contracted and deviated from this historic pattern due to the pressure of time. Political expertise outside the government was provided by the Finanspolitiska Rådet. This board is formally independent from the government, and is tasked with monitoring financial policies. Other commissions provided additional policy-making expertise during the financial crisis, perhaps most notably the so-called Globalization Council, introduced in 2007. This commission includes representatives from government, labor and employers' groups, the scientific community and public life, who provide policy alternatives to the government aimed at strengthening the Swedish position in times of enhanced competition in world markets. In its May 2009 final report, the Council presented its views on reforming the Swedish economy to deal with the global crisis.<sup>46</sup>

<sup>45</sup> Local governments in the Swedish model are responsible for approximately 45% of public expenditures and collect over 60% of their revenues from taxes. The Swedish model is in these terms highly decentralized, and the local governments have high fiscal independence. cf. OECD, "Country Note: Sweden," *Government at a Glance* (Paris: 2009): 1.

<sup>46</sup> The final report: Globalization Council, "Bortom krisen. Om ett framgångsrik Sverige i det nya globala ekonomin," Ds 2009: 21, <http://www.sweden.gov.se/content/1/c6/12/68/57/e04110d0.pdf>; the English version "Beyond the Crisis. How Sweden can succeed in the New Global Economy" is available at: <http://www.sweden.gov.se/content/1/c6/13/10/85/91191b9c.pdf>; more information about the

The Swedish government coordinates crisis management multilaterally. On the one hand, crisis management in Sweden has consistently been embedded into the EU's broader response to the crisis. During the second half of 2009, the Swedish government held the EU presidency, a fact that might help account for the high degree of cooperation within the EU framework. Additionally, Swedish governments are very ambitious in directly implementing EU laws. On the other hand, Swedish cooperation is embedded into the framework of the Nordic countries. Tight historical connections have led the Nordic countries to cooperate intensively in several areas. With the onset of the financial crisis in Iceland, the other Nordic countries agreed to help the Icelandic government. The Swedish (and other Nordic) governments contributed a total of nearly €1.775 billion in loans, with a maturity of 12 years, in the context of IMF negotiations.<sup>47</sup> This measure offered Iceland access to long-term financing and supported the country's policy response to the crisis.

The Swedish Riksbank too is intensively involved in multilateral negotiations over responses to the global financial crisis, and has pursued particularly intensive cooperation with the European Central Bank.

Furthermore, the Swedish government, in collaboration with governments from Denmark, Finland and Norway, coordinated a multinational response providing crisis assistance to Latvia. As early as December 2008, the Nordic countries announced they would support Latvia's economic and financial reform efforts. The four Nordic countries provided credits to the Baltic nation of up to €1.8 billion, contingent on the successful implementation of the reform program.<sup>48</sup>

Finally, the Swedish government has cooperated closely with the IMF. Up to the end of 2009, no curtailments of Swedish policy due to IMF support programs were observable. Quite in contrast, the IMF report on Sweden's response to the crisis was quite complimentary of the government's policies.<sup>49</sup>

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work of the Globalization Council (and more documents) is available at:

<http://www.sweden.gov.se/sb/d/8616> (accessed November 10, 2009).

<sup>47</sup> Ministry of Finance, "Nordic Countries Sign Agreement on Credits to Iceland of 1.775 billion Euro," *Press Release*, July 1, 2009. The first signal for this policy was presented by the Swedish government on January 15, 2009, <http://www.regeringen.se/sb/d/11403/a/118602> (accessed November 20, 2009).

<sup>48</sup> cf. the joint statement available at: <http://www.regeringen.se/sb/d/11218/a/118091> (accessed October 12, 2009).

<sup>49</sup> cf. IMF, "Sweden 2009: Staff Report."

### 3. Policy Content

- How large is the stimulus package as expressed as a percentage of GDP (including compensations to those hit particularly hard by the crisis through social/labor policies)?
- The stimulus is spread over a period of how many years?

Scope of stabilization and stimulus policies

Obviously, it is difficult to estimate the exact magnitude of all stabilization and stimulus policies implemented since the beginning of the financial crisis. In a first step, the government introduced various measures to stabilize the Swedish financial system. During the winter of 2008 – 2009, the government then introduced various measures to stimulate the broader Swedish economy.

The composition and overall magnitude of the policies aimed at stabilizing the Swedish banking system, introduced in October 2008, are described in Table 1.

Table 1: Actions taken to stabilize the financial sector (2008)

	Administration / Authority	SEK Billion
Deposit Guarantee	RGK	1,000
Guarantees for banks and other financial institutions	RGK	1,500
Immediate stability measures for banks (Stability Funds)	RGK	15
Capital support to solvent banks	RGK	50
Foreign Loans	RGK	13
Measures toward export industries I (allowances)	SEK	5
Measures toward export industries II (increased loans)	SEK	100
Measures toward export industries III (various guarantees)	SEK	450
Measures toward export industries IV (guarantees)	EKN	350

Measures targeted to small firms	ALMI	3
Guarantees for EIB	RGK	25
Measures for automotive industries	RGK	28
Sum		3,539

Abbreviations: RGK = Riksgälden (National Debt Office), SEK = Svensk Exportkredit (Swedish Export Credit Corporation), EKN = Exportkreditnämnd (Swedish Export Credit Authority), ALMI = ALMI Företagspartner AB (ALMI, a public organization tasked with enhancing the growth of small business), EIB = European Investment Bank.

Source: Bergström, Clas, 2009: *Finanskrisen och den svenska krishanteringen under hösten 2008 och vintern 2009*, Rapport till Finanspolitiska Rådet, 37.

By the end of 2009, it was not yet clear how far Swedish banks would be forced to take advantage of stabilization policies such as the public guarantees. In total, the financial support measures amount to a potential sum of 7.7 percent of Swedish GDP.<sup>50</sup> Several credit rating agencies estimated that budget expenditures for Swedish bank support would reach five percent to 10 percent of GDP. However, the latest forecast from Riksgälden estimates that public expenditure, even in the worst case, will amount only to two percent of GDP.<sup>51</sup>

During the winter of 2008 and the spring of 2009, the government launched a variety of measures aimed at stabilizing the economy. First, the government relaxed financial policy requirements and reduced the structural surplus from two percent to one percent of GDP.<sup>52</sup> Second, in September 2008, the

<sup>50</sup> IMF, "Sweden 2009: Staff Report," 20.

<sup>51</sup> Riksgälden, "Not even an economic disaster in the Baltic States would generate great costs for the Swedish government," *General Government Borrowing – Forecast and Analysis* 2009:2 (Stockholm: 2009): 16-17, <https://www.riksgalden.se/dokument/Dokument-eng/Riksg%C3%A4ldskontoret%20&%20statsfinanserna/Artiklar%20ur%20statsuppl%C3%A5ningsrapporten/2009/Not%20even%20an%20economic%20disaster%20in%20the%20Baltic%20States%20would%20generate%20great%20costs%20for%20the%20Swedish%20government.pdf> (accessed November 20, 2009).

<sup>52</sup> The premium pension system, introduced in the reforms of the late 1990s, was reclassified to the private sector in 2007. This was the reason for the abovementioned reduction. cf. OECD, "Economic Survey: Sweden," (2008): 53.

government prepared the budget bill and included several expansionary measures. This fiscal stimulus was estimated to total approximately one percent of GDP.<sup>53</sup> Two-thirds of these measures were related to tax cuts. The corporate income tax rate was reduced from 28 percent to 26.3 percent (0.21% of GDP). Additionally, the general employers' contribution rate was reduced from 32.42 percent to 31.42 percent (0.22% of GDP). The government increased the threshold over which state income tax must be paid, and the in-work tax credit was enlarged<sup>54</sup> (these measures combined comprised an estimated 0.45 percent of GDP). The basic tax deduction was raised for people aged 65 or above (0.05% of GDP), and employers' contribution rebate for youth employees was enlarged (0.02% GDP). Finally, the government increased spending in a variety of sectors such as infrastructure, education and social security. The largest item is a rise in transport infrastructure spending (0.11% of GDP).

With an additional January 2009 bill, the government introduced the so-called ROT-avdrag. This measure was aimed at stabilizing the domestic construction industry by reducing taxes. Additionally, the government expanded labor market programs. This policy was further strengthened in the spring 2009 budget. At this time, the central government gave grants to local government aimed at stabilizing employment and social services. The structural surplus rule was again reduced by 0.3 percent of GDP.<sup>55</sup> The overall size of these various measures is impressive. The government estimates the magnitude of the tax reductions and spending increases to total approximately SEK 83 billion, or approximately 2.7 percent of GDP.<sup>56</sup>

The 2010 budget bill, presented in September 2009, follows the trajectories of previous stimulus measures and increases discretionary policies to a remarkable extent. The government declared it would (temporarily) increase grants to local government even further than planned in the spring budget. Additionally, the earned income tax credit was further expanded, as was investment in active labor market policy and education. The government estimated that these measures combined would amount to 1.6 percent of GDP in 2009 and 1.1 percent in 2010.<sup>57</sup>

Beyond these measures, the Swedish welfare state provides substantial automatic stabilizers. Due to high levels of public spending and the relative

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<sup>53</sup> OECD, "Economic Survey: Sweden," (Paris: 2008): 30.

<sup>54</sup> The center-right coalition introduced an earned income tax credit immediately after the 2006 elections, and it has been in effect since January 2007.

<sup>55</sup> The government expected tax reductions in the construction industry to amount to SEK 3.5 billion per year. However, SEK 1 billion of the tax reduction was consumed during the first three months of operation; cf. Dagens Nyheter, October 5, 2009, [www.dn.se](http://www.dn.se).

<sup>56</sup> PROP 2009/10: 1, 41.

<sup>57</sup> cf. Swedish Government, *The Swedish Reform Program for Growth and Jobs. Annual Progress Report* (Stockholm: 2009): 9.

generosity of various social security schemes, the amount of these automatic stabilizers is very high compared to other OECD countries.<sup>58</sup> The government states that “Sweden has provided the largest fiscal stimulus of all the OECD countries reported.”<sup>59</sup>

Most of the stimulus is spread over a period from 2009 until 2011. Approximately one-third of the total measures are explicitly temporary. The government has emphasized the need to observe future economic developments and react immediately with further stimulus policies if needed.

- How is stimulus spending distributed across sectors? How and to what extent is the financial sector supported (e.g., through loans, guarantees, capital injections)?
- Which industrial and structural policies (e.g. corporate tax cuts, subsidies, company bail-outs) can be observed?
- What kinds of measures target the expansion of public spending on infrastructure? Which ones are designed to sustain business and consumer spending?
- Are policies in support of businesses adequately targeted and delineated (e.g., at creating employment, supporting competitive firms)?

Targeting and coverage of policy tools

The Swedish government introduced a variety of measures to stabilize the financial system. As shown above in Table 1, the government has provided far-reaching guarantees for banks. Drawing on lessons learned in the early-1990s banking crisis, the government has actively intervened in the financial system.

Specifically, the government and the Riksbank launched the following measures as a part of their efforts to stabilize the financial system.<sup>60</sup> The Riksbank reacted quickly and began to cut the repo rate in huge steps.<sup>61</sup> As late as September 2009, the repo rate was 4.75 percent; this was cut to one percent in February 2009, and finally down to 0.25 percent on July 8, 2009. The Riksbank immediately began full acceptance of covered bonds, and lowered the minimum credit rating requirements for long-term securities pledged as collateral. Additionally, the Riksbank set up new three-, six- and 12-month loan facilities to facilitate banks’ access to long-term funds, and established a new temporary credit facility using commercial paper as collateral to facilitate the supply of credit for non-financial companies. The National Debt Office (Riksgälden) issued Treasury bills and invested the funds raised in covered bonds to boost covered (mortgage) bond markets. Finally, the Riksbank granted emergency liquidity assistance facilities to

<sup>58</sup> OECD, “Employment Outlook” (Paris: 2009): 29 ff.; Fiscal Policy Council 2009.

<sup>59</sup> PROP 2009/10:1, 23.

<sup>60</sup> This section draws from IMF, “Sweden 2009: Staff Report”; OECD, “Economic Survey Sweden,” 2008; Riksgälden, “Riksgäldens åtgärder för att stärka stabiliteten i det finansiella systemet,” Dnr 2009/1651, (Stockholm: 2009).

<sup>61</sup> cf. Homepage of Riksbank, <http://www.riksbank.com/templates/Page.aspx?id=12182> (accessed November 13, 2009).

Kaupthing Bank Sverige AB and Carnegie Investment Bank AB (for a total of approximately SEK 5 billion). Kaupthing Bank was later liquidated, while the Carnegie Investment Bank's license was revoked.

Beyond these measures, which were aimed at improving the liquidity of the Swedish krona, the Riksbank implemented measures to improve foreign exchange liquidity. The Riksbank and the U.S. Federal Reserve set up temporary reciprocal swap facilities worth a total of \$30 billion. A separate swap facility was established with the European Central Bank. The Riksbank offered new dollar term loan facilities, and worked to boost the country's foreign currency reserves through borrowing by the National Debt Office (for a total of SEK 100 billion).

The government and the Riksbank intervened in the financial system in order to increase stability and trust. The government swiftly increased the deposit guarantee from SEK 250,000 to SEK 500,000.<sup>62</sup> In October 2008, the government approved a debt guarantee scheme for medium-term borrowing by banks and mortgage institutions. The total amount of the guarantee was set at SEK 1.5 trillion. An institution applying for the guarantee would pay fees and be subject to restrictions on remuneration for senior management. This guarantee program is valid until the end of April 2010. In November 2008, Swedbank AB, Swedbank Pypotek AB and Volvofinans Bank AB took advantage of this guarantee scheme. After February 2009, this list lengthened somewhat to include SBAB, Carnegie Investment Bank AB, SEB AB and Sparbanken Gripen AB. By the end of September 2009, the total amount of effective guarantees amounted to SEK 308 billion, with 90 percent of this amount used by various institutions affiliated with Swedbank.<sup>63</sup>

Beyond this guarantee, the government introduced a recapitalization scheme intended to be used by banks and other credit institutions. The governments' capital takes the form of shares or hybrid capital. Participating institutions are subject to restrictions on remuneration for senior management. In October 2008, the National Debt Office was empowered to take over troubled banks, in cases when a bank's capital falls below 25 percent of the regulatory requirement, and serious systemic risk exists. By the end of September 2009, the Riksgälden had used this power only in the case of Carnegie Investment Bank. Finally, the government introduced a stabilization fund aimed at supporting the financial system (and potentially

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<sup>62</sup> The amount of the new deposit guarantee is slightly above the €50,000 agreed upon by EU finance ministers in 2008, cf. OECD, "Economic Survey: Sweden" (Paris: 2008): 27.

<sup>63</sup> For the details cf. Riksgälden, "Riksgäldens åtgärder för att stärka stabiliteten in det finansiella systemet" (Stockholm: 2009): 3, <https://www.riksalden.se/Dokument/Riksgaldskontoret%20och%20statsfinanserna/Rapporter/Ovriga%20rapporter/Riksgaldens%20atgärder%20för%20att%20stärka%20stabiliteten%20i%20det%20finansiella%20systemet.pdf> (accessed November 15, 2009).

forestalling future financial market turmoil). The fund is drawn from annual fees paid by banks and other credit institutions. The stated goal is to increase the fund's holdings up to 2.5 percent of GDP by 2023, but the government announced it may also contribute to the growth of the fund in the nearer-term future.

Beyond the stabilization of the financial sector, the government implemented various measures to stimulate the Swedish economy. Recently, the IMF stated that most of the measures fell on the tax side.<sup>64</sup> However, the government also implemented some immediate industrial and structural policies.

Among the most prominent of these were the stabilization measures focusing on Sweden's car industry, taking the form of a three-pillar package launched in December 2008. First, the government earmarked SEK 3 billion in research and development funds for the auto industry. Second, the government provided loan guarantees worth SEK 20 billion for companies developing green technologies. Third, the government provided short-term loans (six months) for auto companies with liquidity problems. The second and third items of the crisis package were administered by the National Debt Office.<sup>65</sup> In contrast to other European countries, no specific subsidies were allocated to the automotive industries. Social partners negotiated local agreements allowing temporary layoffs, which are normally prohibited in Sweden. These agreements combine a reduction in wages and a reduction in working hours, and do not include public subsidies. The agreements are valid until March 31, 2010, and are focused mainly on the automotive industries.<sup>66</sup>

The government also introduced various policies to expand infrastructure investment (especially in the 2009 budget and in the "Measures for Jobs and Adjustment" bill passed in January 2009). Additional investment in transportation infrastructure will total approximately 3.4 percent of GDP in the 2009 – 2011 period. These expenditures will be focused on maintenance works and expanding the public transportation system.<sup>67</sup> The Fiscal Policy Council has been critical of these measures, arguing that they were not grounded in a systematic analysis of future transportation demands.

Aside from the public infrastructure investments, the government also de-

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<sup>64</sup> IMF, "Sweden 2009: Staff Report," 32.

<sup>65</sup> Rikard Forslind and Karen Helene Ullveit-Moe, "Industripolitik för den svenska fordonsindustrin," *Rapport till Finanspolitiska Rådet* 3 (2009): 12, <http://www.finanspolitiskaradet.se/download/18.1166db0f120540fe0498000209107/090609+Forlind+Moe.pdf> (accessed November 15, 2009).

<sup>66</sup> Cf. EIRO 2009: "Agreement on temporary layoffs reached in manufacturing," <http://www.eurofound.europa.eu/eiro/2009/03/articles/se0903019i.htm> (accessed October 12, 2009).

<sup>67</sup> Fiscal Policy Council, "Swedish Fiscal Policy," (Stockholm: 2009): 154, <http://www.finanspolitiskaradet.se/download/18.75eae27c1223be52adb800042157/Swedish+Fiscal+Policy+2009.pdf> (accessed November 20, 2009).

cided to apply stimulus funds to education, increasing the amount dedicated to student loans and investing in vocational training outside the framework of active labor market policies. This implies increased numbers of places for students in the regular (municipal) education system.<sup>68</sup>

Sweden's approach to crisis management has in general been a mix of spending on infrastructure and public employment on the one side, and tax or fiscal policies aimed at stimulating business and private consumption on the other. According to the most recent estimates as of the time of writing, tax reductions targeted at business and consumers represented the majority of all measures implemented since fall 2008.<sup>69</sup>

Lars Calmfors, chairman of the Fiscal Policy Council, recently criticized some of the tax reductions (such as the increase in the earned income tax credit) for being targeted at increasing labor supply rather than at stimulating demand. Additionally, Calmfors criticized the fact that two-thirds of all stimulus measures were permanent (earned income tax credit, tax cut for senior citizens, increased resources for the judicial system) rather than temporary. Hence, most tax reductions were not aimed specifically at stimulating demand during the global recession, but instead permanently change the structure of the Swedish tax system.<sup>70</sup>

- Are stimulus measures influenced/limited by pre-crisis development strategies (e.g., industrial policies) or have novel/additional (e.g., environmental) policy objectives been inserted?
- Is the response to the crisis grounded in a broader developmental perspective (i.e., crisis as development opportunity) or predominantly short-term political constituency logic?
- Do stimulus policies address prevailing structural deficits and future growth potential?

Development as an objective of stimulus policies

To a certain extent, crisis management measures taken at the beginning of the financial crisis were defensive. The first measures implemented were aimed at stabilizing the financial system. Following this, a support package designed to preserve the domestic car industry was passed. However, some innovative aspects can be observed. First, the government introduced environmentally focused policies as part of its support for the auto industry. It formulated ambitious policy goals to reach climate targets, and in combination with the crisis measures, increased spending on research and introduced

<sup>68</sup> Fiscal Policy Council, "Swedish Fiscal Policy," (Stockholm: 2009): 70, 174-176.

<sup>69</sup> IMF, "Sweden 2009: Staff Report."

<sup>70</sup> Lars Calmfors, "Economic Policy in the Crisis," Jönköping International Business School (2009), Slides available at: <http://www.finanspolitiskaradet.se/download/18.29115341124be3e7f31800019/Calmfors+2+november+2009.pdf> (accessed November 22, 2009).

green car rebates. Second, the government combined crisis measures with political goals to strengthen the Swedish model's international competitiveness. In this respect, the decrease in specific taxes and in the amount of employers' social contributions can be noted. To a certain extent, the introduction of the earned income tax credit and its expansion during the crisis will reduce the tax burden and increase employment. In these respects, the government's policies reflect new policy goals.

Traditional policy goals have also been strengthened, particularly in the case of education. Since the crisis of the early 1990s, there has been a broad political consensus around fostering education in Sweden. The government's current anti-crisis measures reflect this consensus, and have accordingly led to increased expenditure. It should be noted that the opposition has argued for even higher levels of spending for education and research.

Similarly, the government's strengthening of welfare services may be judged as a traditional policy measure. However, the central government's financial injection may be interpreted as contradictory, as the original goal of the center-right government was to decrease public employment levels. The government changed its policy stance during the crisis, and sought to stabilize employment in public welfare services. However, it should be noted that the government has not yet abandoned its goal of deregulating welfare markets.

- Has the stimulus included "buy national" clauses? Have import-restricting mechanisms been newly established or re-established?
- Has the country's executive/central bank manipulated the exchange rate or intervened in the foreign exchange market (if so, in which direction)?
- Have there been measures to prop up export industries (e.g., tax rebates, direct export subsidies)?

National bias and protectionism

Between the outbreak of the financial crisis and September 2009, there were no observable signs of protectionist measures. This policy stance follows the Swedish model's traditions of far-reaching openness. It should be noted that the Swedish government even undermined domestic military industries, buying military equipment abroad in order to save money. This decision was roundly criticized by the opposition.<sup>71</sup>

The Riksbank has not visibly intervened in currency markets so as to manipulate the exchange rate directly. However, the Riksbank's monetary policy has come under pressure. Since the deregulation of the capital markets and the change from a fixed currency regime to a floating regime, the Riksbank

<sup>71</sup> "Början till slutet för den svenska försvarsindustrin," *Dagens Nyheter*, October 27, 2009, [www.dn.se](http://www.dn.se) (accessed October 27, 2009).

has not used its policy instruments to defend the value of the krona. Hence, the Riksbank allowed the national currency to depreciate significantly after the crisis began. This might enhance recovery and boost exports, but the risk of domestic bubbles may endanger long-term prosperity. Therefore, the

question of Swedish membership in the EU's Economic and Monetary Union (EMU) is currently back on the political agenda.<sup>72</sup>

As shown in Table 1, the government invested huge amounts of money in fall 2008 in order to strengthen export industries. However, no direct subsidies for the automotive industry were offered. In contrast, the government tried to improve loan conditions for all exporting firms, and aimed at circumventing potential credit crunches. In this respect the Swedish government avoided the difficult task of differentiating between various export industries, instead providing policy instruments targeted at the export sector as a whole.

- Which labor market policies have been enacted (e.g., unemployment benefits, rise in public-sector employment)?
- Which social policies have been included (e.g., expansion of support, additional investment in health and education system)?
- Which measures have been taken to support purchasing power (e.g., consumer checks, tax cuts, cash transfers)?

Social protection

The Swedish welfare state is very broad, providing automatic stabilizers in times of economic turmoil. Since September 2008 (and the implementation of the 2009 budget bill), several social policy reforms have been enacted, with most of the direct labor market measures increasing spending on active labor market policies. This trend was strengthened in January 2009 with an extra bill, again with the spring budget bill, and finally again with the 2010 budget bill as presented in September 2009.

The government estimates that the increased resources will contribute to an increase of 4,000 work-experience placements and places in practical skills development programs in 2010, and that an additional 8,000 individuals will receive expanded public employment services in the form of intensified intermediation services (coaching). Labor market training will increase by about 1,000 places during 2010. Combining all new investments from fall 2008 to fall 2009, the government expects an increase of about 21,500 places in active labor market programs, above and beyond the already high number

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<sup>72</sup> cf. for example: Anders Olshov, "Dags att gå över till stabil europeisk penningpolitik," *Dagens Nyheter*, October 16, 2009, <http://www.dn.se/opinion/debatt/dags-att-ga-over-till-stabil-europeisk-penningpolitik-1.975562> (accessed November 15, 2009).

of participants.<sup>73</sup> In total, the government estimates that the number of persons enrolled in active labor market programs will increase from 85,000 to 250,000 by 2012—thus, the share in relation to the total labor force may increase from approximately two percent to five percent.<sup>74</sup> Furthermore, the government has devoted an additional SEK 1 billion to the Public Employment Service. This is intended to secure the quality of this authority's work, which has been challenged by the sharply increasing numbers of unemployed.

Recent active labor market reforms target several distinctive groups, with special policy measures aimed at addressing the traditional problems of high youth unemployment and labor market segregation for immigrants.

The public employment share is high in Sweden. Following the change in government in 2006, the center-right coalition had intended to decrease public employment levels. However, the international crisis endangered public employment in social services, which is provided by local and regional governments. As a result of increasing complaints from local and regional governments, the government decided in the spring 2009 budget to introduce central government grants to local governments, a program that was later expanded in the fall 2009 budget. The government proposed a temporary increase of SEK 10 billion in local government grants for 2010. The regional governments, which are responsible for health care, received SEK 1 billion in temporary grants during 2009. The government has emphasized that these measures are highly cost-effective. However, the central government has said it would monitor how local and regional decision makers use the money.

In 2007, the government reformed the country's unemployment insurance program. As a result, employees' contributions rose and unemployment benefits decreased. It is estimated that 450,000 Swedes subsequently decided to leave the unemployment insurance plan (Sweden has a non-obligatory "Ghent system").<sup>75</sup> As a consequence of the financial turmoil and the increasing number of unemployed, the government reformed unemployment insurance rules to a certain extent, despite criticism (the new rules came into force July 1, 2009, and were slated to remain valid until December 31, 2009). Membership fees were marginally reduced to SEK 50, and the wait-

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<sup>73</sup> In 2007, active labor market policies absorbed approximately 3.5% of the total labor force. The government spent 1.12% of GDP for these measures; see OECD, "Employment Outlook" (2009): 281).

<sup>74</sup> "Tio extra miljarder till arbetsmarknadspolitik," *Dagens Nyheter*, April 21, 2009, [www.dn.se](http://www.dn.se) (accessed April 21, 2009).

<sup>75</sup> Cf.: EIROonline, "New Temporary Unemployment Insurance Rules Adopted" (2009), <http://www.eurofound.europa.eu/eiro/2009/07/articles/se0907019i.htm> (accessed November 25, 2009).

ing time before eligibility for payments was reduced from 12 months to six months. These reforms were aimed at preventing a situation in which increasing numbers of unemployed lacked unemployment insurance coverage. However, trade unions criticized the change for not going far enough, and started a signature campaign pressing for broader reform. The Fiscal Policy Council has argued in favor of making unemployment insurance cyclically dependent, increasing benefits in times of recession and reducing them in “normal times.”<sup>76</sup> However, beyond the limited reforms, the government did not react to its critics on this issue by the end of 2009.

Finally, the government increased resources for the judicial system. Since 2006, the center-right government has provided SEK 2.5 billion to the judicial system. With the fall budget bill, a further increase in spending is envisaged (SEK 2.6 billion for 2010). These resources will increase employment levels and support efforts to reduce crime in Sweden.<sup>77</sup>

The central government’s support for local and regional governments is expected to stabilize social service employment. This is intended to maintain the high quality of health services and education. “In the long run, well-functioning schools are the best measure for improving the labor market situation for young people,” the government has said.<sup>78</sup> Beyond the financing of local and regional activities, the government introduced a temporary increase in education initiatives in September 2009 (adult vocational training/adult education, vocational colleges, and universities). Under current plans, it will invest SEK 2.3 billion in 2010 and SEK 2.2 billion in 2011 in support of these measures.<sup>79</sup>

In addition, the central government provided a temporary increase in funding for student loans, taking effect in January 2010. SEK 131 million will be devoted to this program in 2010, and SEK 148 million for 2011 and 2012 combined. Additionally, the government raised the exempt amount, giving students better ability to improve their financial situation with income in addition to study support. This measure is expected to cost SEK 50 million for 2011 and 2012 combined.<sup>80</sup>

The government introduced a series of tax reductions during the economic downturn. The in-work tax credit (in effect since 2007, and a cornerstone in the government’s strategy to increase employment) has been significantly expanded. The government plans to invest SEK 10 billion a year in this pro-

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<sup>76</sup> Finanspolitiska Rådet, *Swedish Fiscal Policy. Report of the Fiscal Policy Council 2009, Principal Conclusions and Summary*, (2009): 2.

<sup>77</sup> PROP 2009/10:1, 33.

<sup>78</sup> PROP 2009/10: 1, 30.

<sup>79</sup> PROP 2009/10: 1, 30.

<sup>80</sup> PROP 2009/10: 1, 32.

gram in the 2010 – 2012 period. This earned-income tax credit is targeted at all wage earners; however, the tax reduction is most significant among lower income groups. Estimates put the total 2007 – 2009 reduction in employee and employer taxes associated with this measure at SEK 71 billion, with a budgetary cost reaching two percent of GDP in 2009.<sup>81</sup> As well as reducing marginal tax rates, this scheme also lowers average tax rates. In 2006, the average income tax rate for a nursing assistant was 28.9 percent, for example. This rate was reduced in 2007 to 25.1 percent, in 2008 to 24.3 percent and finally in 2009 to 23.3 percent.<sup>82</sup>

Beginning in 2009, employer social security contributions were cut by one percentage point across the board. Additionally, social security contributions for the self-employed were reduced by five percentage points, effective in 2010. Other regulatory reforms were aimed at improving social security for entrepreneurs.

Additional tax reductions were targeted at pensioners. The stock market decline in 2008 will activate a balancing mechanism in 2010, which will result in reduced pensions. To counteract pensioners' loss of income, the government introduced income tax cuts for people 65 or older at the beginning of 2010. The government estimates that this reform will cost SEK 3.5 billion.

In January 2009, the government introduced the so-called ROT-avdrag (taking effect July 1, 2009). This measure halves taxes on work done in households, with a ceiling of SEK 50,000 per taxpayer. The customer can subtract this portion of the taxes directly from the bill, while the craftsman or entrepreneur has to apply for compensation from the Swedish Tax Agency (Skatteverket). The government planned to spend SEK 3.5 billion on this measure between July 2009 and July 2010. However, the Skatteverket had already disbursed SEK 1 billion after the program's first three months of operation. This measure has mainly served to stimulate the building industry. Household services are only infrequently the recipients of compensation.<sup>83</sup>

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<sup>81</sup> OECD, "Economic Survey: Sweden" (2008): 78.

<sup>82</sup> PROP 2009/10: 1, 27.

<sup>83</sup> "Rotavdraget spränger miljardvallen," *Dagens Nyheter*, October 5, 2009, [www.dn.se](http://www.dn.se) (accessed October 5, 2009).

## 4. Implementation

- Does the government actively communicate and justify the rationale/goals of its stimulus policies to the public?
- Over time, how has the public responded to the government's management of the crisis (e.g., consumption/investment trends, public opinion polls)?

Political  
communication

At the beginning of the international crisis, the government hesitated somewhat in making public its positions on adequate crisis management. Since September 2008, when the government first included expansionary measures in its budget bill, it has been keen to defend its policies in the public sphere. The same is true for the extra bill adopted in January 2009. Further measures were integrated into regular budget bills. Traditionally, the budget is intensively debated in the Swedish public. Hence, the government was forced to defend crisis management in parliament and in the public sphere. In summer 2009, the government's position was boosted by a positive evaluation of its crisis measures by the IMF.<sup>84</sup>

The approach to crisis management has been contested in the Swedish public. However, the electorate seems on the whole to approve the governing coalition's overall policy mix. Since the outbreak of the crisis, opinion polls have registered increasing support for the coalition. The Conservative Party in particular has benefited from this development. Prime Minister Fredrik Reinfeldt too has seen his approval levels rise. In contrast to Social Democrat Party Chairwoman Mona Sahlin, the top opposition candidate for the 2010 election, Reinfeldt seems to have earned public trust for his capabilities and personal commitment.<sup>85</sup> Given the logic of contemporary Sweden's party competition, this difference may be important during the 2010 electoral campaign.

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<sup>84</sup> IMF, Sweden 2009: Staff Report.

<sup>85</sup> "Förtroendet ökar stort för MP-topp," *Dagens Nyheter*, November 7, 2009, [www.dn.se](http://www.dn.se) (accessed November 15, 2009); cf.: [http://www.synovate.se/Templates/Page\\_195.aspx](http://www.synovate.se/Templates/Page_195.aspx) for further information.

- How large has the time lag been between adoption and implementation of selected major stimulus components?
- What are the reasons for delay in implementation (e.g., legal barriers, insufficient capacities, corruption)?
- Have sectoral or regional interest groups influenced the workings of policy implementation in any way?

Modes and time  
frame of  
implementation

Policy implementation is efficient in Sweden, even in times of financial turmoil. As mentioned above, decisions on financial system stabilization measures were made over the course of eight days, and these decisions were then implemented quickly. Other crisis measures were embedded into the regular implementation pattern of the Swedish state.

In order to enhance efficiency, the government established institutions in October 2008 intended to coordinate crisis measures between the central and local governments. The duties of these special institutions range widely, including coordination of labor market policies, coordination of infrastructure investments and coordination of educational initiatives.<sup>86</sup>

Some national institutions were confronted with difficult tasks from the very beginning of the financial turmoil. Perhaps first among these was the National Debt Office (Riksgälden). This authority's traditional function has been to borrow in the market from households, firms and financial institutions. Today, this authority has been given the responsibility for the bank guarantee, as well as other types of financial institution support and guarantees. In effect, many financial institutions now have a business relationship with Riksgälden while simultaneously being subject to the exercise of this authority's new duties. The Fiscal Policy Council has recommended transferring these supervision and control powers to a new and independent agency.<sup>87</sup>

Potentially complicating its activities, the Swedish government has had to shoulder the double task of managing the EU presidency and shaping its domestic crisis response. However, the government has evidently met both challenges successfully. In terms of implementation, we can observe no exceptional time lags. As mentioned above, in the case of capital transfers to regional and local governments the central government has said it would monitor the funds' use quite attentively. Implementation in Sweden is not

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<sup>86</sup> cf. Näringsdepartementet, "För ett starkare Sverige. Regionala samordnare i samarbete med den svenska regeringen" (Stockholm: 2009), <http://www.regeringen.se/content/1/c6/13/39/99/5073330f.pdf> (accessed November 12, 2009).

<sup>87</sup> cf. Fiscal Policy Council, *Swedish Fiscal Policy. Principal Conclusions and Summary* (Stockholm: 2009): 18-19.

hampered by corruption; indeed, the country leads international rankings in terms of low reported levels of corruption.<sup>88</sup>

Policy implementation in Sweden is efficient and experienced. In this respect, no sectoral or regional interest groups were able to influence policy implementation in any noteworthy sense. Corporatist representation of interest groups in official circles has declined since 1992, which means that labor and employers groups have lost influence over policy implementation. Nevertheless, these social partners have retained a presence on several advisory boards.

- Beyond emergency stand-by programs with the IMF, has the government collaborated with other governments or international organizations in implementing its response to the crisis?

International or regional cooperation

As mentioned above, the Swedish government has collaborated intensively with foreign governments, perhaps most so in the case of the Nordic countries, but also with respect to the broader European Union.

This collaboration has included cooperation on implementation as well as on policy-making. Through the Nordic Cooperation framework, for example, the Swedish government participates in a multilateral monitoring process evaluating the success of reform in Latvia. The Nordic Cooperation is normally a rather loose framework for collaboration, mostly in cultural matters, but it has broadened toward economic and welfare issues since the early 1990s, with particular emphasis on the Baltic countries. During the financial crisis, the cooperative approach proved effective in dealing with Iceland as well as Latvia.

The Swedish government and the Riksbank are also integrated into the multilateral framework of the IMF. Thus, implementation of crisis measures is regularly monitored and evaluated by the IMF.

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<sup>88</sup> See for example: <http://www.worldaudit.org/corruption.htm> (accessed November 15, 2009); OECD, “Economic Survey: Sweden” (Paris: 2008): 20.

## 5. Funding, Tax and Monetary Policies

- Has the government initiated tax reductions/incentive schemes?
- Have these been aimed at the private and/or the corporate, domestic or the foreign sectors?

Tax policies in support of stimulus/stabilization

Sweden's crisis response has relied to a great extent on tax incentives, which are mainly aimed at domestic private and business consumption. As described above, some recent tax policies have proved controversial in the economics community. While the government emphasizes that the tax reductions will stimulate domestic demand, some observers have argued that tax policies in fact have been designed to shift the domestic tax structure.

One Swedish innovation has been the opportunity given to firms with liquidity problems to defer tax and social security contributions for a limited period (a maximum of two months in a given year), subject to an interest rate charge. The intention is to directly address a possible credit crunch for Swedish firms and to provide some respite to financially constrained firms. Policymakers hope the measure will prevent temporary layoffs.<sup>89</sup>

- What kind of policies did the central bank contribute to the national crisis response? Which unconventional measures were used to fight the crisis?
- If an independent national monetary policy is not feasible, were there substituting measures in the country's exchange rate policy?

Monetary and currency policies in support of stimulus/stabilization

As in most other OECD countries, the Swedish central bank intervened quickly after the crisis became apparent, and injected huge amounts of money into the financial market. In addition, the Riksbank supported and partially prepared the Swedish government's first stabilization measures. In October 2008, the government increased a variety of financial institution guarantees, injected together money into the financial system in conjunction with the Riksbank, and prepared the legal framework for takeovers of insolvent banks (see above).

The Riksbank elected to lower the repo rate quickly, in substantial steps. Additionally, the Riksbank (in accordance with government policy, we might assume) decided not to intervene to counteract the capital outflows which depreciated the national currency. Hence, the Swedish krona was

<sup>89</sup> cf. OECD, "Employment Outlook" (Paris: 2009): 107.

allowed to float (in contrast to the early stages of crisis management in the 1990s).

Two “unconventional” measures can be identified. First, the Swedish central bank intervened quickly to stabilize Kaupthing Bank Sverige AB, a Swedish subsidiary of the Kaupthing Bank of Iceland, which was struggling to meet its payment obligations. The Riksbank, working with the Swedish Financial Supervisory Authority, provided emergency liquidity support. Kaupthing’s Swedish subsidiary was subsequently bought by Ålandsbanken on March 27, 2009, without intervention by the National Debt Office, and the full amount of the liquidity support was repaid to the Riksbank.<sup>90</sup>

The Swedish central bank followed a similar strategy in stabilizing Carnegie Investment Bank AB, injecting emergency liquidity support in the midst of the crisis. However, on November 10, 2008, the Swedish Financial Supervisory Authority reported serious failures in the bank’s risk management structure. In cooperation with the Riksbank, the National Debt Office took over the bank, playing the special role assigned to it by the government’s crisis management framework. On February 11, 2009, the National Debt Office agreed to divest itself of Carnegie Investment Bank AB shares, selling them to private-sector owners.<sup>91</sup>

Since 1999, the Swedish central bank has been totally independent from the Swedish government. Therefore, the Riksbank could act independently. However, Riksbank officials have repeatedly emphasized the intensive cooperation characterizing all crisis measures implemented since fall 2008, not only with other foreign central banks but also with other authorities in Sweden (Riksgälden, Finansstyrelsen) and the Swedish government.

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<sup>90</sup> Johan Molin, “Ten Years as an Independent Central Bank. How Has the Riksbank Handled the Crisis?” (Stockholm: 2009): 16, [http://www.riksbank.com/upload/Dokument/rb\\_090911\\_eng.pdf](http://www.riksbank.com/upload/Dokument/rb_090911_eng.pdf) (accessed November 15, 2009).

<sup>91</sup> Johan Molin, “Ten Years as an Independent Central Bank. How Has the Riksbank Handled the Crisis?” (Stockholm: 2009): 16-17, [http://www.riksbank.com/upload/Dokument/rb\\_090911\\_eng.pdf](http://www.riksbank.com/upload/Dokument/rb_090911_eng.pdf) (accessed November 15, 2009).

- Relative to conditions at the outset of the crisis, does stimulus funding have a solid foundation in monetary policy or in bond/credit markets?
- Is the program part of the normal budget/integrated into the budgetary cycle, or is it financed primarily from sources outside of the formal budget?
- Is there cross-level burden-sharing between center and regions (e.g., debt issuance, fund transfers)?
- Is financial aid given to banks/companies/households in a discretionary way or based on well-defined formulas (e.g., conditionalities)?
- Did the government make credible commitments to terminate its expansionary fiscal and monetary policies under (what kind of) post-crisis conditions?

Credibility of  
funding  
mechanisms

As described above, Sweden entered the period of financial turmoil in a sound fiscal situation. Thus, the country's flexibility to pursue discretionary measures has been comparatively high.

Stimulus funding has mostly been embedded in the normal budgetary policy-making process. Hence, the impact of stimulus measures is directly observable. The government is forecasting that the actual fiscal balance will be negative in 2009, showing a deficit of 2.2 percent of GDP, and again in 2010, where the deficit be 3.4 percent of GDP. However, the cyclically adjusted fiscal balance will remain positive in 2009 (at 1.4 percent of GDP) and even in 2010 (0.2 percent of GDP).<sup>92</sup> These calculations rest on a variety of assumptions, of course. At this date, it remains highly uncertain how public tax receipts will develop over the next year.

Major stimulus measures are integrated into the budget. However, measures directed at the stabilization of the financial system are partially excluded. In this respect, it remains unclear how future turbulence in global financial markets will impact Sweden's budgetary situation. Currently, the situation in the Baltic states is very important for Sweden. Although the IMF reported in March 2009 that Swedish measures to aid stability in domestic and foreign financial systems totaled 7.7 percent of the country's GDP, several credit rating agencies have estimated public expenditure to support Swedish banks to be between 5 percent and 10 percent of GDP. However, the latest Riksgälden analyses estimate total public expenditure for bank support to be much lower, at approximately at 2 percent of GDP.<sup>93</sup>

<sup>92</sup> cf. Lars Calmfors, "Economic Policy in the Crisis," Jönköping International Business School (2009). Slides available at: <http://www.finanspolitiskaradet.se/download/18.29115341124be3e7f31800019/Calmfors+2+november+2009.pdf> (accessed November 22, 2009).

<sup>93</sup> Riksgälden, "Not even an economic disaster in the Baltic States would generate great costs for the Swedish government," *General Government Borrowing – Forecast and Analysis 2009:2* (Stockholm: 2009): 16-17, <https://www.riksgalden.se/dokument/Dokument-eng/Riksg%C3%A4ldskontoret%20&%20statsfinanserna/Artiklar%20ur%20statsuppl%C3%A5sningssrapporten/2009/Not%20even%20an%20economic%20disaster%20in%20the%20Baltic>

Burden-sharing between center and regions is a pillar of the Swedish model. As noted above, the regional and central governments each perform important tasks in the Swedish welfare state, and both have the right to levy taxes. Hence, taxes are divided between the central government and the regions. Nevertheless, since the fiscal reforms of the 1990s, regional and local governments have had to follow tight budgetary balance rules. This was responsible for the central government's fiscal transfers in 2009. Without this fiscal support, regional and local government would not have been able to fulfill budgetary rules without cutting costs, which in most cases would have led to a reduction in employment.

One lesson from the early-1990s banking crisis was that well-defined formulas enhance trust and predictability. Therefore, the Swedish government and the Riksbank formulated clear guidelines for intervention from the very beginning of the crisis.

One peculiarity of the Swedish case is the Riksbank's policy of presenting its internal decision-making processes to the public. In this way, the bank has both sought to increase its own transparency and to increase stability in the financial system at large, as all market participants can thus follow its decisions.<sup>94</sup>

The issue of exit strategies has been intensively debated in the Swedish public sphere. As of the time of writing, the government had made no clear announcement as to when or how it would reduce or conclude operation of its discretionary policies. This lack of guidance has been criticized by the Fiscal Policy Council and other economists.

The Riksbank too has thus far avoided describing its own exit strategies. However, since summer 2009, official reports and official statements have at least mentioned the imperative to plan a consistent exit strategy. The Riksbank closely monitors economic developments, and has referred in public announcements to progress in Norway and Australia, where repo rates have already started to increase slightly.

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[%20States%20would%20generate%20great%20costs%20for%20the%20Swedish%20government.pdf](#) (accessed November 20, 2009).

<sup>94</sup> cf. OECD, "Economic Survey: Sweden," (Paris: 2008): 31.

## 6. Feedback and Lesson-Drawing

- Have there been revisions or additions to the original policy packages or a sequence of distinct stimulus policies in response to unexpected new developments?

Policy feedback and adaptation

Sweden's response to the financial crisis followed a somewhat inconsistent pattern. Stabilization measures for the financial system were designed and implemented quickly, and were comprehensive and clearly formulated. However, stimulus policies were rather hesitantly implemented. The economy's decline in GDP was deep during 2008 and 2009. The emergency signals (as described above) were clear. Nevertheless, the government was careful in drafting comprehensive stimulus packages. The first reactions, contained in the 2009 budget bill (passed in fall 2008) relied mainly on tax reductions. Reacting to sharp criticism from the public sphere, the government then implemented support measures for the automotive industry (December 2008), an increase in spending on active labor market policies, and additional stimulus for infrastructure and housing (January 2009). The spring 2009 budget was again cautious in terms of further spending increases. In the 2010 budget (passed in September 2009), the government further increased spending. One important measure, demanded throughout 2009 by a number of observers, was an increase in central government grants to local governments.

This pattern is somewhat surprising, as the financial situation could have allowed the Swedish government to act earlier to counteract the economic downturn. Despite positive evaluations of the country's crisis management by various observers,<sup>95</sup> the Fiscal Policy Council, and especially its chairman, Lars Calmfors, have criticized the government's delays (among other issues). Calmfors stated that the 2010 budget is not only designed to counteract the economic crisis, but also to prepare the ground for the 2010 election campaign.<sup>96</sup>

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<sup>95</sup> IMF, "Sweden 2009: Staff Report."

<sup>96</sup> Jenny Stiernstedt, "Det är en krisbudget-och en valbudget," *Dagens Nyheter*, September 20, 2009, <http://www.dn.se/nyheter/politik/det-ar-en-krisbudget-och-en-valbudget-1.956699>, (accessed November, 20, 2009).

- Has major institutional reorganization/capacity-building been undertaken in financial supervision?
- Do we find new institutions that were not in place prior to the crisis (e.g., bad banks)?

Institutional restructuring

Major institutional reorganization occurred in conjunction with the immediate stabilization of the financial system. One key approach represented a deviation from the lessons learned in the 1990s, when a Bank Support Authority (Bankstödsnämnd) was established to handle banks with major liquidity problems and address their solvency problems. During the current crisis, no such authority was established. Instead, the government charged the National Debt Office (Riskgälden) with these tasks.

Indeed, the National Debt Office was given administrative responsibility over many of the major tasks associated with stabilizing the financial system. Inside this authority, something like a “bad bank” was created, as the authority has the right to take over toxic assets from banks with liquidity problems.

One institutional innovation was the establishment of a national stability fund, introduced in connection with the October 2008 stabilization plan. The fund is primarily financed by a one-off government contribution (SEK 15 billion) and mandatory fees paid by financial institutions. Additional public money will flow into the fund when the effect of the current financial crisis is fully observable. Under current plans, fund holdings will increase over the next 15 years until they reach 2.5 percent of GDP. However, the fund is designed to be tapped during future financial crises.<sup>97</sup>

A further institutional innovation is the establishment of coordinative institutions that are developed to coordinate crisis measures between the central and local governments.<sup>98</sup>

<sup>97</sup> cf. Fiscal Policy Council, *Swedish Fiscal Policy*, (Stockholm: 2009): 43-44

<http://www.finanspolitiskaradet.se/download/18.75eae27c1223be52adb800042157/Swedish+Fiscal+Policy+2009.pdf> (accessed November 12, 2009).

<sup>98</sup> cf. Näringsdepartementet, “För ett starkare Sverige. Regionala samordnare i samarbete med den svenska regeringen,” (Stockholm: 2009)

<http://www.regeringen.se/content/1/c6/13/39/99/5073330f.pdf> (accessed November 12, 2009).

## 7. Tentative Economic Impact

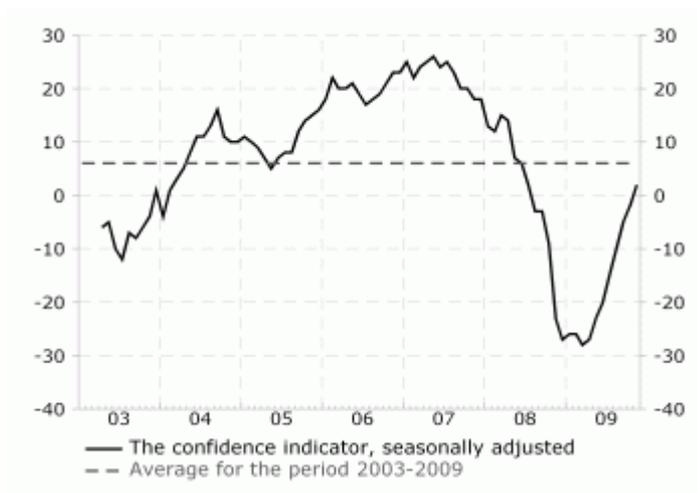
- What do major economic performance indicators tell us about the short-term effectiveness of the crisis response (e.g., growth rate, unemployment rate, industrial output, private consumption, consumer/producer confidence, inflation, exports, bank balance sheets, credit squeezes)?
- How has the political logic of crisis management (i.e., crisis as an opportunity to broaden political support) worked out for the major decision-makers so far? How has the reputation of major government leaders at the center of the crisis response evolved (e.g., based on polls, election results, backing within their political party)?

Economic and political effectiveness of the crisis response

It is too early to make systematic judgments as to the efficiency of the reform measures applied to date. In November 2009, the first signs of recovery were observable in Sweden, as elsewhere in Europe. Several sources report that the Swedish economy is on a moderate growth track. Swedish exports have increased slightly, but private consumption still shows negative growth. The government and the OECD both have forecast a rather slow recovery, with the danger of persistently high open unemployment. The government and the IMF argue that financial risks remain in effect, given the uncertainties in the Baltic states (as well as in the United States).

Positive signs of recovery are observable in the business sector. After the strong decline in business confidence during the financial crisis, Swedish business confidence has increased rapidly since early 2009. This positive perspective on the near-term future is mainly attributable to high levels of confidence in the retail trade and private service sectors, however. In contrast, confidence indicators in the manufacturing sector and the building industry are still declining, albeit more slowly than before.

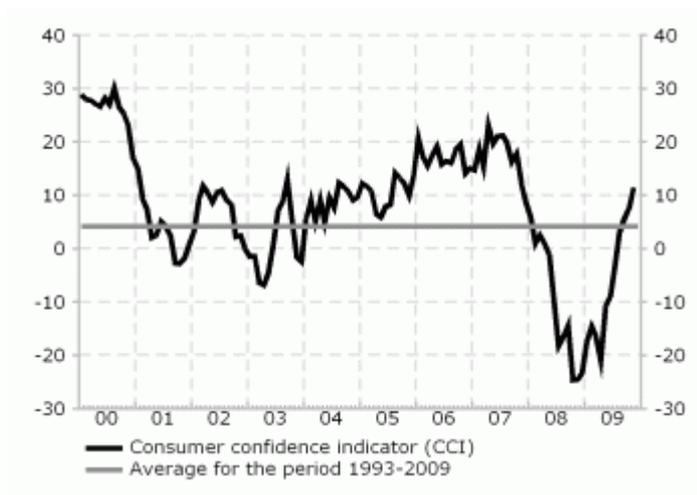
Figure 2: Economic tendency indicator Swedish business



Source: Konjunkturinstitutet 2009, <http://www.konj.se/sidhuvud/inenglish/archives/archive/economic tendency survey business and consumer november 2009.5.8615c78125078c8d338000768.html> (accessed November 25, 2009).

The consumer confidence indicator is even stronger than the business confidence indicator. However, behind this positive trend we can observe that approximately 50 percent of all Swedish households state that the economic situation is worse today than it was a year ago. They show a more negative opinion of the economy's current situation than is historically normal.<sup>99</sup>

Figure 3: Consumer confidence indicator



Source: Konjunkturinstitutet 2009, <http://www.konj.se/sidhuvud/inenglish/publications/economic tendency survey/consumertendency survey.106.32d4db7210df50fec2d80009647.html> (accessed November 25, 2009).

<sup>99</sup> For details see Konjunkturinstitutet, <http://www.konj.se/sidhuvud/inenglish.4.2f48d2f18732142c7fff4422.html> (accessed November 25, 2009).

Even in the financial sector, short term forecasts report positive trends. However, as the Finansinspektionen recently stated: “Of the approximately SEK 50 billion the banks reported in credit losses in 2009, more than half comes from the banks’ operations in the Baltics. The shaky macroeconomic situation in the Baltic countries means that there is considerable uncertainty about how large future credit losses will be.”<sup>100</sup> However, as mentioned above, Riksgälden estimates of the concrete danger faced by Swedish institutions are more optimistic than those of the IMF. The solvency of life insurance companies has returned to pre-crisis levels.

Several economic institutions have forecast a slow recovery for the Swedish economy. According to these forecasts, one of the most pressing risks is the situation in the Baltic states. However, no signs of a credit squeeze for the domestic market has yet emerged.

The most pressing problem, according to these predictions, may be persistent unemployment in the near-term future.<sup>101</sup>

To be sure, the center-right coalition government itself has benefited somewhat from the economic crisis, at least from a political perspective. While public support for the government declined following the election in 2006, it has steadily increased since September 2008. An opinion poll executed recently reported that 76 percent of all Swedes judge Prime Minister Fredrik Reinfeldt to be a competent crisis manager. Even trade union members, by a clear majority (60 percent to 40 percent), favored the prime minister over the Social Democratic chairwoman, Mona Sahlin.<sup>102</sup>

This increased level of public support for the prime minister strengthened the whole coalition. According to the latest opinion polls, the center-right coalition could end up gaining public support relative to the left-leaning parties. As of October 2009, the left block still had a slight polling advantage (0.7 percentage points), but this lead had declined steadily since September 2008’s high of 19.1 percentage points.<sup>103</sup> Since the outbreak of the global

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<sup>100</sup> Finansinspektionen, “Summary,” *Risks in the Financial System*, (Stockholm: November 10, 2009): 2, [http://www.fi.se/upload/90\\_English/20\\_Publications/10\\_Reports/2009/risks\\_financial\\_system4.pdf](http://www.fi.se/upload/90_English/20_Publications/10_Reports/2009/risks_financial_system4.pdf) (accessed November 25, 2009).

<sup>101</sup> These forecasts have been challenged by some economists. cf. Bengt Assarsson, “Ekonomi blir batter än vad Riksbank spar,” *Dagens Nyheter*, September 3, 2009, [www.dn.se](http://www.dn.se) (accessed September 15, 2009).

<sup>102</sup> cf. “Skop: Reinfeldt skickligast,” *Dagens Nyheter*, October 29, 2009, [www.dn.se](http://www.dn.se) (accessed October 29, 2009). The same growing levels of support have been associated with Conservative Minister of Finance Anders Borg. cf. Synovate, *Förtroendet för Börg och Östros* (Stockholm: 2009), [http://www.synovate.se/upload/U568\\_Förtroende%20för%20Borg%20och%20Östros\\_okt\\_2009.pdf](http://www.synovate.se/upload/U568_Förtroende%20för%20Borg%20och%20Östros_okt_2009.pdf) (accessed November 25, 2009).

<sup>103</sup> Synovate väljarbarometer, [http://www.synovate.se/Templates/Page\\_195.aspx](http://www.synovate.se/Templates/Page_195.aspx) (accessed November 25, 2009).

crisis, conflicts between the parties in government have also declined. In September 2009, the government seems to be cohesive and to have a firm level of support in the public sphere.

- Is there early evidence that the structure of the economy will change (e.g., greater role of the state, changes in sectoral shares in GDP)?
- Could old structural imbalances be aggravated? Can we already identify new structural imbalances? Have previously existing imbalances been tackled?

Structural distortions

There is no evidence that the structure of the economy will change specifically due to the financial crisis. The decline in public employment observable since the 2006 change in government may be arrested by the additional grants to local governments. There are also signs that the role of the automotive industry in Sweden will be further reduced in the relatively near-term future. This reduction, if it occurs, will not mark a deviation from the long-term trend, however. The Swedish model underwent a comprehensive restructuring during the past decade. Strong export industries are no longer located in manufacturing, but in financial services and information technology. The global financial crisis is not responsible for structural change in the Swedish economy. However, it may have enhanced ongoing structural change.

In sum, the structural composition of the Swedish model is a strong state embedded in dynamic and mostly deregulated markets. The center-right government intends to diminish the role of the state, although this may be delayed for a short time. The government has additionally implemented crisis response measures which will explicitly enhance competition. The expansion of the earned income tax credit during the last year signals that the government aims to decrease the tax load further. It remains to be seen whether this strategy, in conjunction with increases in spending due to the crisis, will allow the government to stabilize the budget in the near-term future.

## 8. Concluding Remarks

The Swedish economy is small and open to foreign markets and developments. Consequently, Sweden is highly vulnerable to external economic disturbances. The economic crisis is still unfolding, and we should be cautious in making statements about the country's overall success in crisis management.

Nevertheless, we can draw conclusions as to some Swedish peculiarities.

First, Sweden entered the crisis in a very sound financial position. Public budgets had to a great extent been consolidated prior to the economic crisis, and since the mid-1990s, fiscal policy requirements had enabled and even forced the various levels of government to make reliable and predictable policy decisions.

Second, management of the financial crisis was influenced by lessons learned in the Swedish banking crisis of the early 1990s. The active measures taken to stabilize the banking sector and the emphasis put on protecting taxpayer money increased confidence in financial institutions. However, in contrast to the situation in the early 1990s, the current financial crisis is international. The highest risks are associated with the activities of Swedish banks in the Baltic states.

Third, the Swedish labor market had expanded up to 2008, but employment has plummeted since the onset of financial crisis. In the near future, increasing levels of unemployment will be the biggest political problem in Sweden. It remains unclear whether the policy measures adopted will halt the increase in open unemployment, or effectively reduce persistent unemployment.

Fourth, enough financial leeway remains to allow additional crisis responses in the near-term future, if necessary. In contrast to common misunderstandings of the contemporary Swedish model, the country's sound public finance stance enables a greater level of discretionary measures than can be supported by most other OECD countries.

Fifth, the future of the Swedish public-private mix is uncertain. The center-right government has acted somewhat inconsistently, as it intended on the one hand to reduce the size of the state, but was on the other hand forced to stabilize public employment in the social services during the crisis. The future of the public-private mix will be influenced by competition between the two political blocs. At the end of 2009, this electoral competition was a neck-and-neck race. The September 2010 election will show whether the current governing coalition can profit from its active management of the crisis. The expansive 2010 budget may additionally work in the center-right coalition's favor.

## Study Context

The Bertelsmann Stiftung has a long tradition of assessing the quality of governance and devising evidence-based policy strategies for decision makers.

The **Transformation Index (BTI)** monitors political management, democratic quality and economic development around the world. The BTI encompasses all 128 developing nations and countries in transition that have a population of more than two million inhabitants, and have not yet attained fully consolidated democracy and a developed market economy.

The **Sustainable Governance Indicators (SGI)** offer a complementary focus on the OECD member states. The SGI evaluate the sustainability of political action in 15 different policy fields (from economy, labor, and education to environment, research and development), the quality of democracy and questions of strategic management capability in each of the 31 OECD countries.

The study *Managing the Crisis* is a joint initiative of the two projects.

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